UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF ILLINOIS

ILLINOIS ENVIRONMENTAL PROTECTION AGENCY, Appellant, v. DONALD SAMSON, Trustee for the Estate of Chemetco, Inc., Appellee,	)	**Case No. 3:11-CV-836 DRH**
IN RE: CHEMETCO, INC., Debtor	)	**Appeal of Proceedings Under Chapter 7 Case No. 01-34066**

BRIEF OF APPELLANT, ILLINOIS ENVIRONMENTAL PROTECTION AGENCY

Appellant, the Illinois Environmental Protection Agency (the "Illinois EPA"), by Lisa Madigan, Attorney General of the State of Illinois, and Assistant Attorney General James L. Morgan, respectfully submits this brief in support of its appeal.

STATEMENT OF BASIS OF APPELLATE JURISDICTION

The District Court has jurisdiction of this appeal of a final order of the Bankruptcy Court authorizing the distribution of proceeds of certain previously approved sales of property of the Bankruptcy Estate pursuant to 28 U.S.C. 158(a)(1) and the Illinois EPA's election to have the appeal heard by the District Court.

STATEMENT OF ISSUES PRESENTED

Whether the Bankruptcy Court, to the detriment of creditors, including the Illinois EPA, erroneously approved the following distributions from the proceeds of sales of estate assets pursuant to the Trustee's December 1, 2010 and April 15, 2011 Notices of Intent to Sell (the "Notices"):

1. the distribution of more than $1 million to Paradigm Minerals and Environmental Services, LLC ("Paradigm") that was contrary to the terms of the Notices and that Paradigm

had no right to receive under the Purchase Agreement approved by the Bankruptcy Court on September 21, 2009 (the "Purchase Agreement") and the Motion to Clarify Purchase Agreement approved by the Bankruptcy Court on May 4, 2010 (the "Motion to Clarify");

2. the distribution of $ 416,195.62 to Industrial Asset Disposition, LLC ("IAD") that IAD had no right to receive under the Purchase Agreement or Motion to Clarify;

3. the distribution of an undetermined amount to Commerce Bank from the proceeds of the sale of estate assets on which it had no security interest; and

3. the distribution of more than $785,000 to the Trustee for claimed operating expenses that were not itemized or substantiated to the detriment of unsecured creditors, including the Illinois EPA.

STANDARD OF APPELLATE REVIEW

The bankruptcy court's factual findings are reviewed for clear error, and its conclusions of law, including mixed questions of law and fact, are subject to *de novo* review. *Stamat v. Neary*, 635 F.3d 974, 979 (7th Cir. 2011).

STATEMENT OF THE CASE

Nature of the Case and Proceedings and Disposition Below

In this Chapter 7 bankruptcy proceeding involving a smelting company, the present appeal by the Illinois EPA challenges the bankruptcy court's decision to approve, over the Illinois EPA's objections, the distribution of nearly 80% of the $3.5 million in anticipated sale proceeds from the debtor's estate. (01-34066 Doc. #1629).The Illinois EPA filed a timely appeal from the bankruptcy court's approval of these payments. (01-34066 Doc.# 1634).

Statement of Facts

This Chapter 7 proceeding involves the liquidation of Chemetco, Inc, a secondary copper and lead smelter. (Record) The current Trustee is Donald Samson.[1] The assets of the estate include thousands of tons of material accumulated by Chemetco over its decades of operations. (01-34066, Doc. # 1142, Motion to Approve Purchase Agreement). These materials raise environmental concerns that the Illinois EPA and the U.S. EPA have sought to address through ongoing civil enforcement proceedings, *United States of America and State of Illinois v. Chemetco, Inc,* 00-670 and 00-677, and prior civil and criminal enforcement cases. The estate liabilities include the proof of claim filed by Illinois EPA for recovery of response costs and more than $40,000,000 in civil penalties in prior enforcement cases as well as US EPA's claim for penalties, compliance costs, and cleanup costs.

Commerce Bank's Security Interest

Commerce Bank filed a Proof of Claim asserting a secured claim of $8,115,147.38 in the Estate's assets (01-34066 Claim 416-1). After the bankruptcy filing, Commerce entered into a settlement with the Estate to reduce the amount of its lien to $5,000,000 and define the property of the Estate to which it applied. (02-03103 Doc. ## 173 and 175). Commerce agreed its lien was limited to the Estate's inventory, parts inventory, accounts receivable, accounts, copper anodes, black copper, zinc material and general intangibles.

The Interim Order

In the pending enforcement case involving the site of Chemetco's smelting operations, the district court entered an order (the "Interim Order") prohibiting any processing of Scrubber Sludge and Slag on the site without a further order of the Court. (00-670 and 677. Doc. #120,

[1] Mr. Samson succeeded Laura Grandy as Trustee on March 9, 2010 (01-34066 Doc.# 1428).

par. 21). The Interim Order also required the Trustee to develop work plans and obtain Illinois EPA approval before selling materials on site, and its attachments included Work Plans for Furnace Cleanup, among other materials. (00-670 and 677, Doc. # 120, pars.5 and 13-16)

Section 363 Sales by Trustee

During the course of this bankruptcy proceeding, the successive Trustees have sought authorization from the Bankruptcy Court pursuant to Section 363 of the Bankruptcy Code (which governs transactions outside the ordinary course of the debtor's operations) to market and/or process on-site materials to pay the millions of dollars in claims filed by the Illinois EPA, the U.S. EPA and others. (01-34066, Doc. # 1142, Motion to Approve Purchase Agreement).

The Trustee's Purchase Agreement with IAD

More than nine months after entry of the Interim Order, the former Trustee and IAD entered into the Purchase Agreement, which included the Interim Order as an exhibit and required IAD to comply with its terms. (01-34066, Doc. # 1142, Motion to Approve Purchase Agreement) After the Trustee addressed some of the bankruptcy court's concerns, it approved the Purchase Agreement on September 21, 2009 (01-34066 Doc. # 1142; 01-34066 Doc.# 1157).[2]

The Purchase Agreement sold some, but not all, of the estate assets to IAD. The items purchased by IAD included the Smelter site and adjacent real estate, as well as materials defined as "Scrap Assets" held by the Estate to IAD (par. 1.1). IAD did not purchase "Excluded Assets" (par. 1.2), including, among other items, Scrubber Sludge (a defined term), Slag (a defined term), "various and sundry feed stocks, 'in-process' materials (i.e., materials contained within or around

[2] A copy of the Purchase Agreement (excluding the Interim Order and other Exhibits) was filed with the Bankruptcy Court as Exhibit A by the Trustee on July 26, 2011 (01-34066 Doc.# 1623).

the existing processing equipment) and sediments and dusts associated with environmental clean-ups," and furnace dust (Purchase Agreement, Schedule 1.2(i) and (ii)).

With respect to category of Scrubber Sludge included within the Excluded Assets, the Purchase Agreement provided that the Trustee could authorize IAD to sell *unprocessed* Scrubber Sludge if IAD incurred all operating costs relating to such sales,[3] in which event it would receive, from the sale proceeds, those operating costs, the Trustee would be paid his actual operating expenses for general site operations, and, until the full balance of the Smelter Purchase Price was paid off, the remaining sales proceeds would be distributed as follows: 5% to the Trustee (to be held in a Trust Fund to pay for environmental cleanups caused by IAD's work), 25% to IAD, 35% to the Estate (which would be applied to reduce what IAD owed on the Smelter Purchase Price), and 35% to Commerce Bank, N.A. "to satisfy its lien against the Slag" (which would also be applied to reduce what IAD owed on the Smelter Purchase Price). (Purchase Agreement, par. 4.2(b)).

The Motion to Clarify

On March 9, 2010, the former Trustee filed a motion to modify the Purchase Agreement, described as a motion to "clarify" the Purchase Agreement (the "Motion to Clarify"), authorizing the Trustee to finalize and enter into an agreement with Paradigm, a new entity formed by the president of IAD. (01-34066, Doc. # 1426). Under the proposed agreement with Paradigm described in the Motion to Clarify, Paradigm would construct and operate at its own expense an on-site facility for processing Scrubber Sludge and Slag to generate "Recovered Materials," as defined in the Purchase Agreement (mostly consisting of certain high-value metals, including

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[3] These costs included the development of Work Plans required under the Interim Order. (Purchase Agreement , par. 4.2(b)).

copper, zinc, lead, tin and nickel, see Purchase Agreement, par. 4.2), and, in exchange, would receive, in lieu of any payment to IAD for its actual operating expenses related to the sale of such Recovered Materials, a flat fee of 30% of the gross proceeds of those sales, with the remaining 70% to be divided according to the percentage formula set forth in the Purchase Agreement. (01-34066, Doc. # 1426, par. 3). The bankruptcy court granted the Motion to Clarify on May 4, 2010. (01-34066 Doc. #1528.)

After approval of the Motion to Clarify, Paradigm never constructed or operated an on-site processing facility, entered into any agreement with the Trustee as contemplated by the Motion to Clarify, or generated any Recovered Materials from estate assets. (Hearing Transcript, p. 14.)

The Notices of Proposed Sales of Estate Assets

On December 10, 2010, and April 15, 2011, the Trustee filed Notices of an intent to sell certain estate assets. The first Notice referred to approximately 4,000 metric tons of unprocessed Scrubber Sludge and 3,500 metric tons of unprocessed "mixed fines" (01-34066 Doc. #1583), and the second notice referred to "approximately 120 tons of furnace cleanup containing metallic, slippage, fines, scrap metal and slag in three grades" (01-34066 Doc. #1608). Each notice specified that proposed sale was of *unprocessed* assets and that the minimum price would be based on a percentage of the "combined assay value for copper plus tin" and "takes into account the processing costs of the purchaser in order to extract the copper and tin from the materials to be sold." (01-34066 Doc. #1583 and 1608). Under these notices, the Estate would not receive any value for zinc, lead, nickel and other materials and valuable metals present in those materials because they had not been processed by Paradigm in any on-site facility to generate Recovered Materials. Each notice recited that the proposed sale was subject to the

terms of the Purchase Agreement approved by the bankruptcy court, and neither made any mention of Paradigm or the Motion to Clarify. (01-34066 Doc. ##1583, 1608.)

The Motion to Allocate the Distribution of Sales Proceeds

On June 23, 2011, the Trustee filed a Motion to Pay Secured Creditor and Allocate Funds from the sales of the furnace cleanup, mixed fines, and Scrubber Sludge (the "Motion to Allocate"). (01-34066 Doc. #1610). In that motion, the Trustee requested court approval to distribute the following amounts for the sales of unprocessed materials pursuant to the Notices:

$1,050,000 to "Buyer"[4] for Operating Expenses;

$785,217.90 to the Trustee for his "Operating Expenses";

$416,195.22 to "Buyer"[5] as its 25% share of Processing Revenue;

$582,673.74 to the Trustee as his 35% share of Processing Revenue;

$582,673.74 to Commerce Bank as its 35% share of Processing Revenue;

$83,329.10 to Escrow Account for future cleanups caused by IAD mismanagement;

$200,000 to Commerce Bank to be deducted from Operating Expenses paid to Buyer and the Trustee.

The Motion to Allocate for the first time asserted that the provisions in the Motion to Clarify altered the terms of the Purchase Agreement by authorizing payments to Paradigm for sales of

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[4] For the two requested payments described here as being payments to IAD, the Motion to Allocate identified the payee as the "Buyer" under the Purchase Agreement (01-34066 Doc. # 1610), which identified the "Buyer" as IAD (Purchase Agreement, pp.1 and 18). The Motion to Clarify did not change this and described Paradigm only as the entity who would perform the contemplated on-site processing. (01-34066 Doc. # 1426, par. 3.) Only in the Trustee's and Paradigm's responses to the Illinois EPA's objection to the Motion to Allocate did they assert for the first time, without documentary support, that Paradigm had succeeded to IAD's interest under the Purchase Agreement and was therefore entitled to any amounts payable to IAD under the Purchase Agreement as well as any amounts payable to Paradigm under the Motion to Clarify. (01-34066, Doc. ## 1617 and 1619). For clarity's sake, this brief generally identifies the approved distributions to IAD and Paradigm without regard to this assignment.

[5] See footnote 4 above.

assets that were not processed by Paradigm in an on-site facility constructed and operated by it. (Pars. 6, 9, and 11). The Motion to Allocate also referred for the first time to a previously undisclosed agreement with Commerce Bank that required it to get $100,000 from any payment of Operating Expenses under the Purchase Agreement (Pars. 12 and 13 and footnotes 1,3 and 5). The terms of that agreement had never been disclosed nor approved by the Bankruptcy Court. Commerce did not mention such an agreement when it amended its claim (01-34066 Claim 416-2).

The Motion reported that the Trustee was still negotiating an agreement to sell the Scrubber Sludge but that the Trustee had negotiated agreements for the Mixed Fines and furnace cleanup, with only furnace cleanup having been shipped. (01-34066, Doc. # 1610, pars. 2, 3, and 5 respectively). The Motion did not specify what amounts were attributable to the sale of Mixed Fines or Furnace Cleanup. Nor did the Motion provide any detail or substantiation for the Trustee's claim for Operating Expenses, including the specific categories of work performed and the actual expenses attributable to each such category.

Illinois EPA objected challenging the assertion that the proposed allocations would benefit the Estate (01-34066 Doc. #1612). The deficiencies noted in the objection included the application of the Motion to Clarify's 30% reimbursement for processing operating expenses to sales of unprocessed materials, the application of the Purchase Agreement to sales not within its purview, the failure to delineate any of the claimed Operating Expenses, and the distribution of sale proceeds to Commerce Bank from assets not subject to its lien (01-34066 Doc. #1612). The Bankruptcy Court overruled these objections, ruling that each of the proposed distributions was authorized under the Purchase Agreement and Motion to Clarify. (01-34066 Doc.# 1629). This appeal followed.

ARGUMENT

The bankruptcy erred by holding that the Purchase Agreement and Motion to Clarify provided for the disputed distributions to Paradigm, IAD and the Trustee, and further erred by authorizing the disputed distribution to Commerce Bank, all of which reduced the potential $3.5 million recovery for the Estate to about $580,000. In particular, the bankruptcy court erred by:

1) making an distribution of $1,050,000 in estate assets to Paradigm that is not authorized by, and is in fact contrary to the terms of, the Purchase Agreement and the Motion to Clarify, where Paradigm never constructed and operated a Processing Facility, never processed any Excluded Materials into Recovered Materials, and never actually entered into an agreement with the Trustee as authorized by the Motion to Clarify;

2) making an distribution of $416,195.52 in estate assets to IAD that is not authorized by, and is in fact contrary to the terms of, the Purchase Agreement, where those assets included materials that IAD was not authorized to sell, and where, for the Excluded Assets that IAD was permitted to sell with the Trustee's approval, IAD was required to bear all related operating expenses before it could recover those expenses plus any percentage share of such proceeds, but the Motion to Allocate reveals that IAD did not incur any such operating expenses.

3) making an distribution of an undisclosed amount of estate assets to Commerce Bank to which it was not entitled by giving it a percentage share of the proceeds from the sale of Furnace Cleanup, on which it did not have a security interest; and

4) making an distribution of $785,217.90 from estate assets to reimburse the Trustee for claimed "operating expenses" that were not within the category of expenses

for which the Trustee was entitled to reimbursement under the Purchase Agreement, and were further undefined, undocumented, and unsubstantiated, including meaningful detail concerning the specific categories of work performed and the actual expenses attributable to each such category.

These distributions are not only unauthorized by the Purchase Agreement and the Motion to Clarify, but also failed to satisfy the standard set by Section 363(b)(1), 11 U.S.C. 363 (b)(1), that sales outside of the ordinary course of the Debtor's business serve the best interests of the Estate and the terms of the sale be fair and reasonable. *In re Apex Oil Company*, 92 B.R. 847, 866 (E.D. Mo. 1988).

I. The Bankruptcy Court Erroneously Held that the Purchase Agreement and Motion to Clarify Authorized Distributing More Than $1 Million in Estate Assets to Paradigm.

The bankruptcy court erred by concluding that the Purchase Agreement or the Motion to Clarify authorized a 30% off-the-top distribution of $1,050,000 to Paradigm where Paradigm had no rights under the Purchase Agreement and the Motion to Clarify authorized such a payment to Paradigm only for sales of Recovered Materials that Paradigm actually processed at an on-site processing facility that it built and operated. It is undisputed that Paradigm never built or operated such a facility and, consequently, never generated any Recovered Materials. It is likewise undisputed that none of the assets sold pursuant to the Notices included any Recovered Materials or other processed materials. Thus, the distribution of more than $1 million to Paradigm represents a clear and unjustified waste of estate assets to the detriment of estate creditors, including the Illinois EPA.

The Purchase Agreement made no mention of Paradigm. And the Motion to Clarify, which was intended to permit to the Trustee to enter into an agreement with Paradigm pursuant

to which it would construct and operate an on-site processing facility to generate Recovered Materials, sought only to "allow the Trustee to pay [Paradigm] the *processing* fee of 30% of the gross revenue from the sale of *Recovered Materials*." (01-34066 Doc.# 1426, Prayer for Relief (emphasis added);see also *id.* at par. 3.) That was the *only* relief sought or granted by the order approving the Motion to Clarify (01-34066 Doc. 1528), and it has no application to the Trustees' sales of *unprocessed* materials under the Notices and, therefore, cannot authorize any distribution to Paradigm. The bankruptcy court's contrary interpretation of the Purchase Agreement and Motion to Clarify is untenable.

Critically, counsel for Paradigm (who is also counsel for IAD and Commerce Bank) admitted at the July 26, 2011, hearing that no Processing Facility was ever built and that no processing by Paradigm, either on-site or elsewhere, ever occurred. To the contrary, the Notices made clear that each of the solicited customers was required to conduct its own processing to recover copper, tin, or other metals from the materials being sold, and that the resulting purchase price reflected that fact. Thus, it was not the case that Paradigm *increased* the value and corresponding price that could be obtained from a sale of estate assets by processing them into higher-value metals qualifying as Recovered Materials. Instead, these assets were admittedly sold for their *lower* value as unprocessed material. And giving Paradigm 30% of that value, when it did not earn that payment according to the terms of the Motion to Clarify, was clearly unjustified.[6]

[6] Also, under the Interim Order incorporated into the Purchase Agreement, no on-site processing of materials was permitted without an order from the District Court approving that processing, which was never sought or granted. Thus, the Trustee could not authorize Paradigm, IAD or anyone else to undertake any processing or to pay them for it.

For the first time at the July 26, 2011, hearing on the Motion to Allocate, counsel for the Trustee and Paradigm both took the position, which the bankruptcy court seemingly adopted, that the Motion to Clarify expanded the definition of Recovered Materials to include *unprocessed* materials, including unprocessed Scrubber Sludge, and authorized Paradigm to sell them and receive a 30% off-the-top share of the proceeds. (Transcript, pp. 7 and 12-13, respectively). That position has no factual basis in the relevant documents, however, and thus provides no support for the bankruptcy court's order. Only the Purchase Agreement, not the Motion to Clarify, dealt with sales of unprocessed Scrubber Sludge and other Excluded Materials, and, as described below, it gave only IAD, not Paradigm, a conditional right to make such sales.

In short, nothing supported the bankruptcy court's approval of a $1,050,000 distribution to Paradigm, and that approval should be reversed.

II. The Bankruptcy Court Erroneously Held that the Purchase Agreement Authorized the Distribution of More Than $400,000 in Estate Assets to IAD.

The bankruptcy court also erred in its conclusion that the Purchase Agreement or Motion to Clarify authorized a distribution of $416,195.52 to IAD from the proceeds of the assets covered by the Notices, representing a 25% flat percentage of the proceeds after other distributions. This is true for two independent two reasons: IAD did not actually undertake the sales of Scrubber Sludge or Furnace Cleanup, and Furnace Cleanup was not among the types of Excluded Assets that the Purchase Agreement permitted IAD to sell.

A. For Excluded Assets that IAD Could Sell with Trustee Approval under the Purchase Agreement, IAD Was Entitled to a Share of the Proceeds Only If It Actually Made the Sales Itself and Performed All of the Related Work.

Under the Purchase Agreement, IAD was entitled to such a share of the proceeds of certain Excluded Assets only if IAD sold those assets with the Trustee's approval and bore all of the actual

operating expenses related to those sales. The materials submitted in connection with the Motion to Allocate disclose, however, that these sales were made by the Trustee, not IAD, and that IAD did not incur any actual operating expenses relating to those sales. IAD therefore was not entitled to any distribution of proceeds from the sale of estate assets pursuant to the Purchase Agreement, and the bankruptcy court's approval of that distribution represented a waste of estate assets to the detriment of estate creditors, including the Illinois EPA.

With respect to those Excluded Assets that the Trustee may authorize IAD to sell under the Purchase Agreement, including unprocessed Scrubber Sludge, Paragraph 4.2(b) of the Purchase Agreement expressly requires IAD to bear all related costs of labor, construction, equipment, marketing and logistics to obtain "a portion of the Processing Revenue as provided herein." In addition, each reference in the Purchase Agreement regarding any sales by IAD of unprocessed Scrubber Sludge required prior approval by the Trustee. (*Id.*, pars. 4.1 and 4.3.) Neither condition was satisfied.

The Motion to Allocate made no mention of any effort by IAD to accomplish the sales. Instead, that motion specifically stated that the "*Trustee* has entered into an agreement with H&H Metals to sell approximately 3,500 tons of mixed fines" which had not yet been shipped, that the *Trustee* had negotiated the sales of Furnace Cleanup, and that the *Trustee* was still negotiating sales of the unprocessed Scrubber Sludge. (01-34066 Doc. # 1610, pars. 2, 3, 5 (emphasis added).) Nowhere did the Motion to Allocate suggest that the Trustee had authorized *IAD* to undertake or consummate those sales or that IAD had done so.

In addition, the Motion to Allocate reflected no operating expenses actually incurred by IAD in connection with the sales covered by the Notices, and the large amount of the operating expenses

claimed by the Trustee (discussed below) compelling indicates that the Trustee, not IAD, incurred any actual operating expenses connected to these sales.[7]

B. The Purchase Agreement Specifically Excluded IAD from Sales of Furnace Cleanup.

The bankruptcy court's order granting the Motion to Allocate also improperly concluded that IAD was entitled to a share of the proceeds from the sale of Furnace Cleanup pursuant to the Purchase Agreement even though Furnace Cleanup was excluded from the list of Excluded Assets that IAD could sell with the Trustee's approval.

The Purchase Agreement identified certain assets as Excluded Assets, generally provided that such assets were excluded from the scope of the agreement, and provided a limited exception to that exclusion for Scrubber Sludge and slag — *not* Furnace Cleanup — that IAD could sell with the Trustee's approval and receive a share of the proceeds (subject to the conditions discussed above). The Motion to Allocate attempted to disregard this express limitation on the category of assets that IAD could sell with the Trustee's approval and obtain a distribution to IAD of a share of the proceeds from the sale of furnace cleanup. The Purchase Agreement clearly precludes any authority for that distribution, however, and in this respect as well the bankruptcy court's order granting the Motion to Allocate was in error.

Schedule 1.2 of the Purchase Agreement identifies "in-process" materials (i.e. materials contained within or around existing process equipment), sediments and dusts associated with environmental clean-ups, and furnace dust as "Excluded Assets." Section 1.2 of the Purchase Agreement provides that such materials "are specifically excluded from the terms of this

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[7] At the July 26, 2011, hearing, counsel for IAD speculated that such costs would be incurred by IAD before the materials could be shipped (Transcript, p. 14), but this falls well short of the type of factual showing necessary to establish that IAD actually bore *all* operating costs relating to these sales and was therefore entitled to a recovery under the terms of the Purchase Agreement.

Agreement."[8] Since these materials were specifically excluded from the Purchase Agreement, IAD could have no right to any share of the proceeds from their sale unless they were specifically included in the limited category of Excluded Assets (namely, Scrubber Sludge and slag) that the Purchase Agreement *specifically* permitted the Trustee to authorize IAD to sell and receive a share of the resulting proceeds. Furnace Cleanup is not in that category, and any distribution to IAD from sales of furnace cleanup therefore constitutes a waste of estate assets to the detriment of estate creditors. The bankruptcy court therefore erred in holding that the Purchase Agreement gave IAD the right to a share of the proceeds from the sale of Furnace Cleanup. Further, because the Motion to Allocate failed to specify what proceeds were obtained from the sale of Furnace Cleanup, if IAD is entitled to any distribution at all the matter should be remanded to the bankruptcy court to give IAD the opportunity to prove, by competent evidence, what share of any sales proceeds were not attributable to the sale of Furnace Cleanup.

III. The Bankruptcy Court Improperly Authorized the Distribution of Estate Assets to Commerce Bank from the Sale of Material on Which the Bank Did Not Have a Security Interest.

The bankruptcy court's order granting the Motion to Allocate also improperly authorized a distribution to Commerce Bank from the proceeds of the sale of estate assets on which the Bank did not have a security interest. One category of estate assets that was not covered by Commerce Bank's lien (and was therefore excluded by the Purchase Agreement from the materials for which Commerce Bank was entitled to a share of any sales proceeds) was Furnace Cleanup. Furnace Cleanup was included in the list of materials described in the April 15, 2011, Notice, but the Motion

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[8] The Copper Furnace Cleanup Solids Work Plan specifically identified Furnace Cleanup as "in-process" materials (i.e. materials contained within or around existing process equipment), sediments and dusts associated with environmental clean-ups, and furnace dust. (00-670 and 00-677 Doc. 120).

to Allocate failed to itemize the amount of sales proceeds attributable to Scrubber Sludge. Thus, a consequence of the bankruptcy court's approval of the Motion to Allocate was to give Commerce Bank an undetermined share of the proceeds from the sale of Furnace Cleanup that Commerce Bank had no right to receive, and for that reason that approval should be reversed.

Although Commerce Bank formulated varying descriptions of the property subject to its lien, none of them validly extended to Furnace Cleanup. Both in the Bank's original claim (01-34066 Claim 416-1) and the settlement agreement it later entered with the Trustee (02-3103 Doc, 173), the items described as being subject to the Bank's lien were Chemetco's "inventory, parts inventory, accounts receivable, accounts, copper anodes, black copper, zinc material and the general intangibles." In its amended claim, Commerce Bank purported to expand the scope of its lien to embrace "scrubber sludge, slag and other metal bearing materials." (01-34066 Claim 416-2, Exhibit A, par. 10). No explanation was given, however, how the lien could be extended to materials which were not in Chemetco's inventory or had been characterized as zinc material, and the Bank's mere filing of a proof of claim asserting such a change did not make that change valid or effective.

As noted above, sales of Furnace Cleanup were not subject to the Purchase Agreement because Furnace Cleanup was not included in the definition of Excluded Assets. Nor was any proof provided by the Trustee or Commerce Bank that Chemetco's "inventory" included materials found on the walls and equipment surfaces of the Foundry Building. The Notice of Intent omits any reference to the presence of zinc in those materials as well. Accordingly, the bankruptcy court's approval of the distribution to Commerce Bank must be reversed. This would, of course, be without prejudice to Commerce Bank's ability to establish, by competent proof, the share of sales proceeds

to which it is properly entitled because those proceeds relate to assets actually covered by its security interest.[9]

IV. The Bankruptcy Court Erroneously Held that the Purchase Agreement Authorized the Distribution of More Than $785,000 in Estate Assets to the Trustee, and Further Erred by Approving that Distribution Without any Itemization or Substantiation for Compensable Expenses Actually Incurred by the Trustee.

Finally, the bankruptcy court erroneously approved the distribution of $785,217.90 in estate asset to the Trustee as supposed "operating expenses" authorized under the Purchase Agreement and Motion to Clarify. The Trustee failed to establish both his *entitlement* to be reimbursed for any operating expenses under the Purchase Agreement and the *amount* of any such reimbursement.

As noted above, the Purchase Agreement required IAD to bear all *sales-related* costs for the sale of materials the Trustee was entitled to sell and further provided that, *if* IAD did so, IAD would receive an off-the-top payment for those operating expenses, and the Trustee would receive an off-the-top payment for his actual operating expenses related to the *general operation of the site*. The Motion to Allocate offers no evidence or other competent factual basis to establish that *any* of the amounts the Trustee wanted distributed to the Trustee for operating expenses fall within the latter category as opposed to the former. Likewise, the Motion to Allocate offers no evidence or other competent factual basis to establish the *amount* of any actual operating expenses that the Trustee actually incurred relating to the latter category. These deficiencies precluded the bankruptcy court from concluding that the Purchase Agreement authorized any distribution of estate assets to the Trustee, and further precluded it from authorizing a distribution in this amount.

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[9] Since a remand is necessary, the Bankruptcy court can inquire further into the previously undisclosed agreement to divert $100,000 from any payment of Operating Expenses to Commerce Bank. See pars. 12 and 13 and footnotes 1, 3, and 5 in the Motion to Allocate, 01-34066 Doc.# 1610).

As the movant on the Motion to Allocate requesting a distribution of estate assets, the Trustee had the burden of proving by sufficient evidence both his right to a distribution and the amount of the distribution justified. He satisfied this burden on neither aspect of this request. Tellingly, the Motion to Allocate, while asking for a distribution for an exact amount — $785,217.90 — was unsworn and unsupported by any affidavits; included no detailed description or other itemization of what the supposed operating expenses were and how much was attributable to each category of work or compensable activity; and was supported by no substantiating business records or other documents. In effect, the Trustee offered nothing more than his own conclusory and wholly unsupported assertion that such expenses were incurred and properly entitled to reimbursement. In the face of the Illinois EPA's objections, that was plainly insufficient.

Courts have repeatedly rejected bankruptcy motions supported by no evidence, mere arguments of counsel, or purely conclusory supporting assertions. See, e.g., *Gorenz v. State of Ill. Dep't of Agriculture*, 653 F.2d 1179, 1184 (7th Cir. 1981); *Phoenix American Life Ins. Co. v. Devan*, 308 B.R. 237, 241 (D. Md. 2004); *In re Trombetta*, 383 B.R. 918, 922 (Bankr. S.D.Ill. 2008); *In re General Search.com*, 322 B.R. 836, 848-50 (Bankr. N.D.Ill. 2005); *In re Okon*, 310 B.R. 603, 609-10 (Bankr. N.D.Ill. 2004) ("But the trustee offered no evidence of the tractor's current value, evidence that could give the court some basis for ruling in his favor. Without evidence, any value the court might assign would be a guess, no better than a shot in the dark. Guessing is not considered a legitimate method for valuing property."). Those principles apply here and require rejection of the requested allocation.

CONCLUSION

For the foregoing reasons, the Court should reverse the bankruptcy court's order granting the Motion to Allocate, rule that neither Paradigm nor IAD is entitled to the distribution of any proceeds

from the sales of estate assets covered by the Notices, and remand the matter to the bankruptcy court to determine, based on satisfactory evidence (including detailed itemization and documentary substantiation), what share of the proceeds of these sales that Commerce Bank is entitled to receive under the Purchase Agreement for materials actually covered by its security interest (not including Furnace Cleanup Solids); and what share of the proceeds of these sales that the Trustee may be entitled to for compensable operating expenses that he actually incurred.

Respectfully submitted,

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September 29, 2011

CERTIFICATE OF SERVICE

The undersigned hereby certifies that on September 29, 2011,a true and correct copy of the foregoing was served electronically upon all parties scheduled upon the Court's ECF Notice List.

/s/ James L. Morgan
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